

Kennedy

McKee & Company LLP Certified Public Accountants

1100 W. Frontview
P. O. Box 1477
Dodge City, Kansas 67801
Tel. (620) 227-3135
Fax (620) 227-2308

JAMES W. KENNEDY, CPA
JAMES R. SHIRLEY, CPA
LU ANN WETMORE, CPA
ROBERT C. NEIDHART, CPA
PATRICK M. FRIESS, CPA
JOHN W. HENDRICKSON, CPA

The Honorable Mayor and City Council
City of Ensign, Kansas

In planning and performing our audit of the financial statements of the City of Ensign, Kansas as of and for the year ended December 31, 2011, in accordance with auditing standards generally accepted in the United States of America, we considered City of Ensign, Kansas's internal control over financial reporting (internal control) as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the City's internal control. Accordingly, we do not express an opinion on the effectiveness of the City's internal control.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies, and therefore material weaknesses or significant deficiencies may exist that were not identified. In addition, because of inherent limitations in internal control, including the possibility of management override of controls, misstatements due to error or fraud may occur and not be detected by such controls. However, as discussed below, we identified certain deficiencies in internal control that we consider to be material weaknesses and other deficiencies that we consider to be significant deficiencies.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A material weakness is a deficiency or combination of deficiencies in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. We consider the following deficiencies in City of Ensign, Kansas's internal control to be material weaknesses:

- Utility billing software for 2011 reflected \$5,709.88 more receipts than were recorded in the general ledger. Reconciliations between the billing software and the general ledger are necessary to ensure that all receipts are properly recorded and deposited. Adjustments to utility accounts receivable should be approved by City Council.
- Bank accounts have not been reconciled since January 2012, the City Treasurer does not review reconciliations, and the Mayor was signing blank checks. It is important to have bank reconciliations done on a timely basis in order for Council to have accurate financial reports. Reconciliations should be reviewed by the City Treasurer to ensure that all reconciling items are appropriate. Checks should be signed after reviewing the supporting documentation for the expenditure.
- Utility accounts receivable have not been reconciled. Reconciliation of accounts receivable is an important process of the utility billing process. Proper reconciliations will show the beginning balance, billing, collections (which should agree with deposits to the bank) and ending balance. Any write-offs of utility billings should be approved by the City Council. Performing these procedures and reviewing these procedures by the City Council will reduce the risk of errors or fraud.

- Receipts are getting posted to the general ledger as a lump sum based on the deposit slip and not being split up among the various revenue accounts and funds. Receipts should be recorded as utility payments (split out water, sewer, and trash), franchise fees, grants, fines, permits, etc. The total deposit should agree to the general ledger and billing software.
- The 3rd Quarter 941 for 2011 was not filed until December 5, 2012. Personnel that process payroll should make sure that all appropriate payroll forms are complete and filed on a timely basis in order to avoid penalties.
- Several expenditures were either incorrectly posted in the general ledger or did not have any supporting documentation to substantiate the expense. The Council should inquire and review bills on a monthly basis and make sure that all bills have appropriate supporting documentation. We noted three specific transactions that we believe should be brought to your attention:
 - \$2,000.00 cash withdrawal on 1/3/2011 from the savings account. We were notified that this transaction was determined to be fraudulent and reimbursed by the City's surety bond in 2012.
 - Check #1003 written on 4/27/2011 in the amount of \$500.00 out of the savings account payable to the City of Ensign. We could not locate any support for this check and could not see that it was deposited to any City bank account.
 - Check #10215 written on 7/15/2011 in the amount of \$200.00 out of the checking account to the City of Ensign for business lunches and dinners. This check was cashed and we could not locate any supporting documentation.

A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. We consider the following deficiencies in City of Ensign, Kansas's internal control to be significant deficiencies:

- No resolution was passed to increase the amount of petty cash on hand for 2012 and the petty cash is not reconciled back to the beginning balance or locked in a secure place when left unattended. Council should adopt a resolution to increase petty cash to the amount deemed necessary and the petty cash box should be reconciled back to the beginning balance daily. Also, the petty cash box should be locked in a file cabinet when left unattended to help prevent theft.
- Reimbursements for mileage and supplies are included in payroll, and very little documentation for the purpose of the trips is provided. Reimbursements for mileage and supplies should be separated from actual payroll and detailed documentation such as receipts for the supplies and mileage, such as date, destination and purpose.
- Minutes for three of the monthly meetings held in 2011 were not readily available for inspection. Minutes serve as a record of the events of the council meetings and should document all important topics discussed and decisions reached. Council minutes can be a crucial document in the event of future legal matters and in documenting compliance with regulatory issues. Minutes should be approved, signed and filed in a permanent record book.
- The minimum rate being charged for water customers was not in agreement with the ordinance. All changes in utility rates should be approved by City Council prior to the rate changes going into effect.

- Due to the limited number of personnel in the office, there is a lack of segregation of duties relating to accounting function of recording transactions in the general ledger and utility billing and utility cash receipts. As a result, errors or irregularities could occur and not be detected on a timely basis by management or the City Council. This condition requires those members of management and the City Council to monitor activities of the City by reviewing financial reports and questioning any unusual activity.

This communication is intended solely for the information and use of management, and the City Council of the City of Ensign, Kansas, and is not intended to be and should not be used by anyone other than these specified parties.

Kennedy McKee & Company LLP

January 8, 2013

Kennedy
McKee & Company LLP Certified Public Accountants

1100 W. Frontview
P. O. Box 1477
Dodge City, Kansas 67801
Tel. (620) 227-3135
Fax (620) 227-2308
www.kmc-cpa.com

JAMES W. KENNEDY, CPA
JAMES R. SHIRLEY, CPA
LU ANN WETMORE, CPA
ROBERT C. NEIDHART, CPA
PATRICK M. FRIESS, CPA
JOHN W. HENDRICKSON, CPA

January 8, 2013

To the Honorable Mayor and City Council and Management
City of Ensign, Kansas

We have audited the financial statements of the City of Ensign, Kansas for the year ended December 31, 2011. Professional standards require that we provide you with information about our responsibilities under generally accepted auditing standards, as well as certain information related to the planned scope and timing of our audit. We have communicated such information in our letter to you dated October 29, 2012. Professional standards also require that we communicate to you the following information related to our audit.

Significant Audit Findings

Qualitative Aspects of Accounting Practices

Management is responsible for the selection and use of appropriate accounting policies. The significant accounting policies used by the City of Ensign, Kansas, are described in Note A to the financial statements. No new accounting policies were adopted and the application of existing policies was not changed during 2011. We noted no transactions entered into by the entity during the year for which there is a lack of authoritative guidance or consensus. All significant transactions have been recognized in the financial statements in the proper period, except that we were not able to satisfy ourselves as to the completeness of utility revenues that all revenues were deposited to the City's accounts.

Accounting estimates are an integral part of the financial statements prepared by management and are based on management's knowledge and experience about past and current events and assumptions about future events. Certain accounting estimates are particularly sensitive because of their significance to the financial statements and because of the possibility that future events affecting them may differ significantly from those expected.

Estimates in the financial statements include budgeted receipts and expenditures. Management's estimate of budget amounts is based on prior actual numbers and on known future conditions. We evaluated the key factors and assumptions used to develop these estimates in determining that they are reasonable in relation to the financial statements taken as a whole.

Certain financial statement disclosures are particularly sensitive because of their significance to financial statement users. The most sensitive disclosure affecting the financial statements is the disclosure of long-term debt in Note D to the financial statements.

The disclosures in the financial statements are neutral, consistent, and clear.

Difficulties Encountered in Performing the Audit

We encountered no significant difficulties in dealing with management in performing and completing our audit.

Corrected and Uncorrected Misstatements

Professional standards require us to accumulate all known and likely misstatements identified during the audit, other than those that are trivial, and communicate them to the appropriate level of management. The following material misstatements detected as a result of audit procedures were corrected by management:

- To allocate cash in the amount of \$168,588.77 between the City's five different funds.
- To reclassify \$101,609.68 of beginning unencumbered cash from the General fund to the Special Highway, Water, Trash, and Sewer funds.
- To reclassify \$13,000 of salary expense from the General fund to the Water fund (\$10,000) and the Sewer fund (\$3,000) to match expenditures shown in the budget.
- To remove \$2,440.00 from accounts receivable in the General fund to conform with the accounting methods being used by the City.
- To separate \$6,953.86 of various tax receipts (motor vehicle, recreation vehicle, etc) that were all posted to ad valorem property taxes in the General fund.
- To reclassify \$2,034.17 of franchise fees from charges for service in the Water fund to franchise fees in the General fund.
- To record accounts payable of \$4,456.07 in the General fund.
- To reclassify \$1,039.70 of salary expense from repairs and parts in the Sewer fund to salaries and wages in the General fund.
- To record water deposits payable of \$1,650.00 in the Water fund.

There were other adjustments made to facilitate proper reporting and minor adjustments to balance cash accounts.

Disagreements with Management

For purposes of this letter, professional standards define a disagreement with management as a financial accounting, reporting, or auditing matter, whether or not resolved to our satisfaction, that could be significant to the financial statements or the auditor's report. We are pleased to report that no such disagreements arose during the course of our audit.

Management Representations

We have requested certain representations from management that are included in the management representation letter dated January 8, 2013.

Management Consultations with Other Independent Accountants

In some cases, management may decide to consult with other accountants about auditing and accounting matters, similar to obtaining a "second opinion" on certain situations. If a consultation involves application of an accounting principle to the governmental unit's financial statements or a determination of the type of auditor's opinion that may be expressed on those statements, our professional standards require the consulting accountant to check with us to determine that the consultant has all the relevant facts. To our knowledge, there were no such consultations with other accountants.

Other Audit Findings or Issues

We generally discuss a variety of matters, including the application of accounting principles and auditing standards, with management each year prior to retention as the governmental unit's auditors. However, these discussions occurred in the normal course of our professional relationship and our responses were not a condition to our retention.

During the course of our audit, we noted several control deficiencies that are communicated to those charged with governance in a separate letter dated January 8, 2013. We also noted certain statutory violations described in Note B to the financial statements.

This information is intended solely for the use of City Council and management of the City of Ensign, Kansas and is not intended to be and should not be used by anyone other than these specified parties.

Kennedy McKee & Company LLP

CITY OF ENSIGN, KANSAS

**FINANCIAL STATEMENTS
with
INDEPENDENT AUDITOR'S REPORT
YEAR ENDED DECEMBER 31, 2011**

TABLE OF CONTENTS

	<u>Page</u>
Independent Auditor's Report.....	1
SUMMARY OF CASH RECEIPTS, EXPENDITURES, AND UNENCUMBERED CASH	3
SUMMARY OF EXPENDITURES - ACTUAL AND BUDGET	4
STATEMENT OF CASH RECEIPTS AND EXPENDITURES - ACTUAL AND BUDGET:	
General Fund.....	5
Special Highway Fund	6
Water Fund	7
Trash Fund.....	8
Sewer Fund.....	9
NOTES TO FINANCIAL STATEMENTS	10

Kennedy
McKee & Company LLP Certified Public Accountants

1100 W. Frontview
P. O. Box 1477
Dodge City, Kansas 67801
Tel. (620) 227-3135
Fax (620) 227-2308
www.kmc-cpa.com

JAMES W. KENNEDY, CPA
JAMES R. SHIRLEY, CPA
LU ANN WETMORE, CPA
ROBERT C. NEIDHART, CPA
PATRICK M. FRIESS, CPA
JOHN W. HENDRICKSON, CPA

INDEPENDENT AUDITOR'S REPORT

The Honorable Mayor and City Council
City of Ensign, Kansas

We have audited the accompanying financial statements of the City of Ensign, Kansas, as of and for the year ended December 31, 2011, as listed in the table of contents. These financial statements are the responsibility of the City's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the *Kansas Municipal Audit Guide*. Those standards and guidance require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As described more fully in Note A, the City of Ensign, Kansas, has prepared these financial statements using accounting practices prescribed or permitted by the State of Kansas which practices differ from accounting principles generally accepted in the United States of America. The effect on the financial statements of the variances between these regulatory accounting practices and accounting principles generally accepted in the United States of America, although not reasonably determinable, is presumed to be material.

Because of the discrepancies between the utility billing software and the general ledger, we are not able to satisfy ourselves as to the amounts recorded as receipts in the enterprise funds beyond deposits made to the bank.

Further, in our opinion, because of the effects of the matter discussed in the second preceding paragraph, the financial statements referred to above do not present fairly, in conformity with accounting principles generally accepted in the United State of America, the financial position of the City of Ensign, Kansas as of December 31, 2011, or the changes in its financial position for the year then ended.

In our opinion, except for the effects, if any, relating to the condition in the second preceding paragraph, the financial statements referred to above present fairly, in all material respects, the cash and unencumbered cash balances of each fund of the City of Ensign, Kansas, as of December 31, 2011, and their cash receipts and expenditures, and budgetary results for the year then ended on the basis of accounting described in Note A.

Kennedy McKee & Company LLP

January 8, 2013

CITY OF ENSIGN, KANSAS

SUMMARY OF CASH RECEIPTS, EXPENDITURES AND UNENCUMBERED CASH

Year ended December 31, 2011

<u>Fund</u>	<u>Beginning unencumbered cash balance</u>	<u>Prior year canceled encumbrances</u>	<u>Cash receipts</u>
Governmental funds:			
General fund	\$ 43,374	\$ -	\$ 83,719
Special revenue funds:			
Special highway	14,152	-	5,062
Proprietary funds:			
Enterprise funds:			
Water	6,100	-	52,257
Trash	41,153	-	16,426
Sewer	<u>38,556</u>	<u>-</u>	<u>13,420</u>
Total	<u>\$ 143,335</u>	<u>\$ -</u>	<u>\$ 170,884</u>

Composition of cash balance:

 Checking account
 Savings account
 Certificate of deposit
 Cash on hand

Total cash

The accompanying notes are an integral
part of the financial statements.

<u>Expenditures</u>	<u>Ending unencumbered cash balance</u>	<u>Add encumbrances and accounts payable</u>	<u>Ending cash balance</u>
\$ 83,341	\$ 43,752	\$ 4,456	\$ 48,208
5,455	13,759	-	13,759
44,837	13,520	1,650	15,170
11,963	45,616	-	45,616
3,650	48,326	-	48,326
<u>\$ 149,246</u>	<u>\$ 164,973</u>	<u>\$ 6,106</u>	<u>\$ 171,079</u>
			\$ 28,264
			121,594
			21,171
			<u>50</u>
			<u>171,079</u>

CITY OF ENSIGN, KANSAS

SUMMARY OF EXPENDITURES - ACTUAL AND BUDGET

Year ended December 31, 2011

<u>Fund</u>	<u>Certified budget</u>	<u>Adjustment for qualifying budget credits</u>	<u>Total budget for comparison</u>	<u>Expenditures chargeable to current year</u>	<u>Variance favorable (unfavorable)</u>
General fund	\$ 115,465	\$ -	\$ 115,465	\$ 83,341	\$ 32,124
Special revenue funds:					
Special highway	17,656	-	17,656	5,455	12,201
Enterprise funds:					
Water	64,650	-	64,650	44,837	19,813
Trash	45,000	-	45,000	11,963	33,037
Sewer	33,900	-	33,900	3,650	30,250
Total	<u>\$ 276,671</u>	<u>\$ -</u>	<u>\$ 276,671</u>	<u>\$ 149,246</u>	<u>\$ 127,425</u>

The accompanying notes are an integral
part of the financial statements.

CITY OF ENSIGN, KANSAS

GENERAL FUND

STATEMENT OF CASH RECEIPTS AND EXPENDITURES - ACTUAL AND BUDGET

Year ended December 31, 2011

	Actual	Budget	Variance favorable (unfavorable)
Cash receipts:			
Taxes:			
Ad valorem tax	\$ 44,631	\$ 44,390	\$ 241
Delinquent tax	448	100	348
Motor vehicle tax	5,547	6,211	(664)
Recreational vehicle tax	129	163	(34)
16/20M truck tax	170	130	40
Intangibles tax	660	660	-
Shared revenue:			
State tax disbursement	15,045	12,000	3,045
Licenses, permits and fees:			
Franchise fees	13,680	9,400	4,280
Licenses	-	100	(100)
Building permits	-	100	(100)
Court income	95	-	95
Gray County fire department	1,300	800	500
Interest	2,014	600	1,414
Miscellaneous	-	100	(100)
Transfers in:			
Trash fund	-	20,000	(20,000)
Total cash receipts	<u>83,719</u>	<u>\$ 94,754</u>	<u>\$ (11,035)</u>
Expenditures:			
Salaries and wages	23,418	\$ 27,000	\$ 3,582
Employee benefits	8,534	3,900	(4,634)
Utilities	12,301	8,000	(4,301)
Insurance	4,576	2,300	(2,276)
Fire department	4,090	3,300	(790)
Dump truck rent	-	3,100	3,100
Office supplies and postage	3,178	1,500	(1,678)
Car wash	818	1,200	382
Community resource building	1,893	2,200	307
Council pay	1,740	1,200	(540)
Due and fees	1,114	1,000	(114)
Park	2,563	600	(1,963)
Publishing	1,492	-	(1,492)
Repairs and maintenance	5,260	5,000	(260)
Mileage	-	2,200	2,200
City hall repairs	50	-	(50)
City streets	520	1,000	480
Miscellaneous	4,639	1,000	(3,639)
Legal and professional fees	7,155	1,000	(6,155)
Street improvements	-	49,965	49,965
Total expenditures	<u>83,341</u>	<u>\$ 115,465</u>	<u>\$ 32,124</u>
Receipts over (under) expenditures	378		
Unencumbered cash, beginning of year	<u>43,374</u>	<u>\$ 20,711</u>	<u>\$ 22,663</u>
Unencumbered cash, end of year	<u>\$ 43,752</u>		

The accompanying notes are an integral part of the financial statements.

CITY OF ENSIGN, KANSAS

SPECIAL HIGHWAY FUND

STATEMENT OF CASH RECEIPTS AND EXPENDITURES - ACTUAL AND BUDGET

Year ended December 31, 2011

	<u>Actual</u>	<u>Budget</u>	<u>Variance favorable (unfavorable)</u>
Cash receipts:			
State of Kansas gas tax	<u>\$ 5,062</u>	<u>\$ 5,230</u>	<u>\$ (168)</u>
Expenditures:			
Salaries and benefits	\$ -	\$ 4,000	\$ 4,000
Fuel	1,506	1,000	(506)
Street repair and maintenance	3,949	11,656	7,707
Miscellaneous	<u>-</u>	<u>1,000</u>	<u>1,000</u>
Total expenditures	<u>5,455</u>	<u>\$ 17,656</u>	<u>\$ 12,201</u>
Receipts over (under) expenditures	(393)		
Unencumbered cash, beginning of year	<u>14,152</u>	<u>\$ 12,426</u>	<u>\$ 1,726</u>
Unencumbered cash, end of year	<u>\$ 13,759</u>		

The accompanying notes are an integral
part of the financial statements.

CITY OF ENSIGN, KANSAS

WATER FUND

STATEMENT OF CASH RECEIPTS AND EXPENDITURES - ACTUAL AND BUDGET

Year ended December 31, 2011

	<u>Actual</u>	<u>Budget</u>	<u>Variance favorable (unfavorable)</u>
Cash receipts:			
Charges for service	\$ 52,257	\$ 52,000	\$ 257
Miscellaneous	<u>-</u>	<u>200</u>	<u>(200)</u>
Total cash receipts	<u>52,257</u>	<u>\$ 52,200</u>	<u>\$ 57</u>
Expenditures:			
Salaries and benefits	10,000	\$ 12,000	\$ 2,000
Repairs, maintenance and supplies	6,497	9,400	2,903
Utilities and telephone	3,662	5,400	1,738
Debt service	16,700	16,700	-
Capital outlay	3,149	10,000	6,851
Sales tax and water protection fee	571	1,000	429
Office supplies	-	500	500
Legal and accounting	4,145	3,000	(1,145)
Licenses and permits	108	-	(108)
Contract labor	5	-	(5)
Analysis and testing	-	350	350
Insurance and bonds	-	1,300	1,300
Miscellaneous	<u>-</u>	<u>5,000</u>	<u>5,000</u>
Total expenditures	<u>44,837</u>	<u>\$ 64,650</u>	<u>\$ 19,813</u>
Receipts over (under) expenditures	7,420		
Unencumbered cash, beginning of year	<u>6,100</u>	<u>\$ 22,021</u>	<u>\$ (15,921)</u>
Unencumbered cash, end of year	<u>\$ 13,520</u>	<u>\$ 9,571</u>	<u>\$ 3,949</u>

The accompanying notes are an integral
part of the financial statements.

CITY OF ENSIGN, KANSAS

TRASH FUND

STATEMENT OF CASH RECEIPTS AND EXPENDITURES - ACTUAL AND BUDGET

Year ended December 31, 2011

	<u>Actual</u>	<u>Budget</u>	<u>Variance favorable (unfavorable)</u>
Cash receipts:			
Charges for service	<u>\$ 16,426</u>	<u>\$ 18,000</u>	<u>\$ (1,574)</u>
Expenditures:			
Trash contractor	11,963	\$ 25,000	\$ 13,037
Transfer to general	<u>-</u>	<u>20,000</u>	<u>20,000</u>
Total expenditures	<u>11,963</u>	<u>\$ 45,000</u>	<u>\$ 33,037</u>
Receipts over (under) expenditures	4,463		
Unencumbered cash, beginning of year	<u>41,153</u>	<u>\$ 41,124</u>	<u>\$ 29</u>
Unencumbered cash, end of year	<u>\$ 45,616</u>	<u>\$ 14,124</u>	<u>\$ 31,492</u>

The accompanying notes are an integral
part of the financial statements.

CITY OF ENSIGN, KANSAS

SEWER FUND

STATEMENT OF CASH RECEIPTS AND EXPENDITURES - ACTUAL AND BUDGET

Year ended December 31, 2011

	<u>Actual</u>	<u>Budget</u>	<u>Variance favorable (unfavorable)</u>
Cash receipts:			
Charges for service	\$ 13,420	\$ 10,500	\$ 2,920
Expenditures:			
Salaries and benefits	\$ 3,000	\$ 6,000	\$ 3,000
Licenses and permits	343	300	(43)
Repairs and maintenance	157	5,500	5,343
Insurance and bonds	-	1,200	1,200
Office supplies and printing	-	700	700
Contract labor	150	200	50
Capital improvement	-	20,000	20,000
Total expenditures	<u>3,650</u>	<u>\$ 33,900</u>	<u>\$ 30,250</u>
Receipts over (under) expenditures	9,770		
Unencumbered cash, beginning of year	<u>38,556</u>	<u>\$ 30,539</u>	<u>\$ 8,017</u>
Unencumbered cash, end of year	<u>\$ 48,326</u>	<u>\$ 7,139</u>	<u>\$ 41,187</u>

The accompanying notes are an integral
part of the financial statements.

CITY OF ENSIGN, KANSAS

NOTES TO FINANCIAL STATEMENTS

December 31, 2011

A. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

This summary of significant accounting policies applied in the preparation of the accompanying financial statements is presented to assist in understanding the City's financial statements which are presented in conformity with the cash basis and budget laws of the State of Kansas. The financial statements and notes are representations of the City's management, which is responsible for their integrity and objectivity.

1. Reporting entity

The City of Ensign is a municipal corporation governed by an elected mayor and five-member council. The scope of the entity for financial reporting purposes is defined as those funds for which the governing body of the City has financial accountability. Financial accountability includes budgetary authority and fiscal management responsibility. Budgetary authority is defined as authority for final approval of budgetary appropriations and revisions. Fiscal management responsibility is control of the collection and disbursement of funds. These financial statements include all funds included in the City's legally adopted budget. The City has no component units.

2. Fund accounting

The accounts of the City are organized on the basis of funds. In governmental accounting, a fund is designated as a sum of money or other resources segregated for the purpose of carrying on specific activities or attaining certain objectives in accordance with special regulations, restrictions or limitations and constituting an independent fiscal and accounting entity. City resources are allocated to and for individual funds based upon the purpose for which they are to be spent and the means by which spending activities are controlled. The following types of funds comprise the financial activities of the City for the year of 2011:

General Fund

This fund is established to account for resources devoted to financing the general services that the City performs for its citizens. General tax revenues and other sources of revenue used to finance the fundamental operations of the City are included in this fund. The fund is charged with all costs of operating the government for which a separate fund has not been established.

Special Revenue Fund

This fund is established to account for the proceeds of specific revenue sources other than special assessments, trust funds, or major capital projects that are restricted by law or administrative action to expenditure for specified purposes.

Proprietary Funds

Enterprise Funds

These funds are established to account for operations that are financed and operated in a manner similar to private business enterprises, where the intent is that the costs of providing goods and services to the general public on a continuing basis be financed or recovered primarily through user charges.

A. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

3. Basis of accounting

Statutory Basis of Accounting. The statutory basis of accounting, as used in the preparation of these statutory basis financial statements, is designed to demonstrate compliance with the cash basis and budget laws of the State of Kansas. Cash receipts are recognized when the cash balance of a fund is increased. Expenditures include disbursements, accounts payable, and encumbrances. Encumbrances are commitments related to unperformed (executory) contracts for goods and services, and are usually evidenced by a purchase order or written contract. For an interfund transaction, a cash receipt is recorded in the fund receiving cash from another fund and an expenditure is charged in the fund from which the transfer is made.

The City Council has adopted a resolution that is in compliance with K.S.A. 75-1120a(c), waiving the requirement for application of generally accepted accounting principles and allowing the City to use the statutory basis of accounting.

Departure from accounting principles generally accepted in the United States of America. The basis of accounting described above results in a financial statement presentation which shows cash receipts, expenditures, cash and unencumbered cash balances, and expenditures compared to budget. A statement of net assets that would have shown noncash assets such as receivables, inventories, and prepaid expense, liabilities such as deferred revenue and matured principal and interest payable, and reservations of the fund balance are not presented. Under accounting principles generally accepted in the United States of America, encumbrances are only recognized as a reservation of fund balance; encumbrances outstanding at year end do not constitute expenditures or liabilities. Consequently, the expenditures as reported do not present the cost of goods and services received during the fiscal year in accordance with generally accepted accounting principles. Capital assets that account for the land, buildings, and equipment owned by the City are not presented in the financial statements. Also, long-term debt such as general obligation bonds, revenue bonds, capital leases, temporary notes, and compensated absences is not presented in the financial statements.

4. Budgetary information

Kansas statutes require that an annual operating budget be legally adopted for the general fund, special revenue funds (unless specifically exempted by statute), debt service funds, and enterprise funds. Although directory rather than mandatory, the statutes provide for the following sequence and timetable in the adoption of the legal annual operating budget:

1. Preparation of the budget for the succeeding calendar year on or before August 1st.
2. Publication in local newspaper on or before August 5th of the proposed budget and notice of public hearing on the budget.
3. Public hearing on or before August 15th, but at least ten days after publication of notice of hearing.
4. Adoption of the final budget on or before August 25th.

The statutes allow for the governing body to increase the originally adopted budget for previously unbudgeted increases in revenue other than ad valorem property taxes. To do this, a notice of public hearing to amend the budget must be published in the local newspaper. At least ten days after publication the hearing may be held and the governing body may amend the budget at that time. There were no such budget amendments for 2011.

A. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

4. Budgetary information (continued)

The statutes permit transferring budgeted amounts between line items within an individual fund. However, such statutes prohibit expenditures in excess of the total amount of the adopted budget of expenditures of individual funds. Budget comparison statements are presented for each fund showing actual receipts and expenditures compared to legally budgeted receipts and expenditures.

All legal annual operating budgets are prepared using the statutory basis of accounting. Revenues are recognized when cash is received. Expenditures include disbursements, accounts payable, and encumbrances. Encumbrances are commitments by the municipality for future payments and are supported by a document evidencing the commitment, such as a purchase order or contract. Any unused budgeted expenditure authority lapses at year-end.

5. Cash and investments

To facilitate better management of City cash resources, excess cash is combined in pooled operating accounts. Each fund's portion of total cash is based on its equity in the pooled cash amount. Cash in excess of current operating needs is invested on a pooled investment basis and earnings thereon are distributed to the general fund and other appropriate funds. Investments consist of certificates of deposit reported at cost, which approximates fair value.

6. Ad valorem tax revenue

The determination of assessed valuation and the collection of property taxes for all political subdivisions in the State of Kansas is the responsibility of the various counties. The County Appraiser's Office annually determines assessed valuation and the County Clerk spreads the annual assessment on the tax rolls. Taxes are levied by November 1 and a lien for all taxes attaches on that same date until the taxes are paid. One-half of the property taxes is due December 20 and distributed to the City by January 20, and the second half is due May 10 and distributed to the City by June 5. The City draws available funds from the County Treasurer's office at designated times throughout the year.

7. Risk management

The City is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. The City purchases commercial insurance to cover property, liability, and worker's compensation claims. There have been no significant reductions in coverage from the prior year, and settled claims resulting from these risks have not exceeded commercial insurance coverage in any of the past three years.

B. COMPLIANCE WITH KANSAS STATUTES

References made herein to the statutes are not intended as interpretations of law, but are offered for consideration to the Director of Accounts and Reports and for interpretation by the legal representatives of the City.

The treasurer did not maintain records to show the amount of money in each fund as required by K.S.A. 10-1118.

The City maintains a listing for each utility deposit showing the date received, name of depositor and the amount; however, it does not pay interest on the utility deposits as required by K.S.A. 12-822.

The City has not published an annual financial statement as required by K.S.A. 12-1608.

C. DEPOSITS AND INVESTMENTS

Policies. The City has no formal deposit and investment policies; however it does follow state statutes. K.S.A. 9-1401 establishes the depositories which may be used by the City. The statute requires banks eligible to hold the City's funds to have a main or branch bank in the county in which the City is located, or in an adjoining county if such institution has been designated as an official depository, and the banks to provide an acceptable rate of return on funds. In addition, K.S.A. 9-1402 requires the banks to pledge securities for deposits in excess of FDIC coverage. The City has no other policies that would further limit interest rate risk.

K.S.A. 12-1675 limits the City's investment of idle funds to time deposits, open accounts, and certificates of deposit with allowable financial institutions; U.S. government securities; temporary notes; no-fund warrants; repurchase agreements; and the Kansas Municipal Investment Pool. The City has no investment policy that would further limit its investment choices. State statutes place no limit on the amount the City may invest in any one issuer as long as the investments are adequately secured under K.S.A. 9-1402 and 9-1405.

Custodial credit risk - deposits. Custodial credit risk is the risk that, in the event of a bank failure, the City's deposits may not be returned to it. State statutes require the City's deposits in financial institutions to be entirely covered by federal depository insurance or by collateral held under a joint custody receipt issued by a bank within the State of Kansas, the Federal Reserve Bank of Kansas City, or the Federal Home Loan Bank of Topeka. At year-end the carrying amount of the City's deposits, including certificates of deposit, was \$171,029. The bank balance was \$172,275, all of which was covered by FDIC insurance.

D. LONG-TERM DEBT

Changes in long-term liabilities for the entity for the year ended December 31, 2011, were as follows:

<u>Issue</u>	<u>Balance beginning of year</u>	<u>Additions</u>	<u>Reductions/ net change</u>	<u>Balance end of year</u>	<u>Interest paid</u>
General obligation bonds:					
Refunding and Improvements					
Issued August 15, 2008					
In the amount of \$163,000					
At an interest rate of 4-5%					
Maturing 09/01/2023	\$ 145,000	\$ -	\$ 10,000	\$ 135,000	\$ 6,700

Current maturities of loan and interest for the next five years and thereafter through maturity are as follows:

	<u>Principal due</u>	<u>Interest</u>	<u>Total due</u>
2012	\$ 10,000	\$ 6,300	\$ 16,300
2013	10,000	5,900	15,900
2014	10,000	5,500	15,500
2015	10,000	5,050	15,050
2016	10,000	4,600	14,600
2017-2021	55,000	16,100	71,100
2022-2023	30,000	2,250	32,250
Total	<u>\$ 135,000</u>	<u>\$ 45,700</u>	<u>\$ 180,700</u>

E. SUBSEQUENT EVENTS

Management has evaluated subsequent events through January 8, 2013, the date on which the financial statements were available to be issued. Management's evaluation concluded that the following subsequent events are required to be recognized or disclosed in these financial statements:

In February 2012 the City executed a lease-purchase agreement for a backhoe and motor grader at a total cost of \$66,600. Lease payments to be made are \$7,957 semi-annually for five years.

In March 2012 the City entered into a grant agreement with the State of Kansas Department of Commerce for the construction of a sewer treatment plant. The projected total cost is \$681,410, of which 50% will be paid from grant funds, and 50% will be financed through the Kansas Department of Health and Environment. The anticipated completion date is March 31, 2014.